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SUBJECT: From Rural to Urban, Part 1: Industry Finds a New Home in Qingyuan

REFERENCE: A) Guangzhou 18102; B) Guangzhou 93

(U) This document is sensitive but unclassified. Please protect accordingly.

¶1. (U) Summary. Qingyuan, Guangdong Province's largest and fastest-growing prefecture, is in the middle of an industrialization boom that will have far-reaching consequences for its urban and rural populations. The Pearl River Delta (PRD) is no longer as cost-competitive as it once was due to a lack of land, energy and water shortages, and rapidly rising wages. Consequently, factories are packing up and moving out. Qingyuan, which lies outside of the PRD, has been successful in courting these factories. Many of the industries that are calling Qingyuan home are notorious polluters, however, including chemical and ceramics companies. These companies also operate on a low margin and will likely leave Qingyuan once its wages rise too high -- a trend that is already starting to happen. Only with a long-term development strategy, perhaps hinging on its burgeoning eco-tourism industry, can Qingyuan avoid a painful hangover down the road. End summary.

¶2. (U) Econoff and EconPolAsst recently visited Qingyuan prefecture, a predominantly rural area stretching from central to north Guangdong Province. The southern reaches of Qingyuan, home to the majority of the population and industry, are only two hours from Guangzhou by bus. Qingcheng City, the largest city in Qingyuan with half a million people, served as our base as we visited nearby factories and more distant villages in southern Qingyuan. This cable explores the nature of Qingyuan's rapid industrialization and its long-term impact. Septel will discuss the concerns of the rural population as they face this incoming tide of industry and urbanization.

Feeding Off the Pearl River Delta

¶3. (U) The sidewalks of Qingcheng's business district at night are overflowing with young and old residents browsing retail stores that sell the latest clothing styles and electronics. Though the per-capita GDP of Qingyuan is only about 40 percent of the Guangdong average, the urban residents of Qingcheng are doing well and are spending their money. This prosperity is relatively new, however -- only in the last few years has Qingyuan changed from being a

backwater to the fastest growing prefecture in Guangdong (Qingyuan's GDP grew at 23.3 percent in 2005). Qingyuan also has the province's fastest growing industrial output, fixed asset investment, retail sales volume, utilization of FDI, gross industrial output, and foreign trade volume.

14. (U) The reasons for this growth are largely geographic: Qingyuan lies just north of the Pearl River Delta (PRD), the center of South China's manufacturing industry that sweeps from Hong Kong to Guangzhou to Macau. Despite continued strong economic growth, the PRD is facing energy and water shortages, rising wage levels, and a land crunch (Reftel B). Factories -- especially low-margin, labor-intensive ones -- are finding that their operations are no longer cost competitive and are looking to relocate. Indeed, during the two years after the Beijing-Zhuhai highway opened, 170 Guangdong factories moved to southern Hunan Province, which borders Guangdong to the north. Twenty percent of new investment in Jiangxi Province, another bordering province, has come from Guangdong.

15. (U) Qingyuan has made attracting these migrating companies its mission. It pitches its low land prices, offers tax incentives, waives water and administrative fees, and offers generous awards to agents that bring investment. An agent can earn up to RMB 100,000 (USD 12,500) by bringing in a large investor. An industrial park representative we spoke with said Qingyuan has attracted 1,600 industrial projects in the last three years, most of which came from the PRD. With a salesman's self-assuredness, he touted the geographic and financial advantages of his park and listed its many satisfied customers. Provincial authorities have helped bring investment to Qingyuan as well, as they are

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eager to keep investment within Guangdong. In the case of a 30,000-employee electronics factory owned by Yi Li Group, which recently moved from Dongguan to Qingyuan, Guangdong authorities facilitated the move by negotiating a deal wherein Dongguan and Qingyuan equally share the new factory's tax revenue.

16. (SBU) As an example of how busy Qingyuan officials are in their efforts to attract investment, Post has on two separate occasions in 2006 been denied in our requests for a series of meetings with Qingyuan offices, apparently because they were accommodating visiting investors. A group of Australian investors were visiting when we last made a request.

But How Long Will the Good Times Last?

17. (SBU) Qingyuan is booming, but if recent history is any guide, its time at the top will be fleeting. Shoetown -- Nike's first OEM manufacturer in China -- recently moved from Guangzhou to Qingyuan because it ran out of room to expand and was facing rapidly rising wages. Indeed, the Guangzhou minimum wage has risen from RMB 450 (USD 56) per month in 2003 to RMB 684 (USD 86) in 2006. And PRD cities are reportedly considering wage hikes of 17-42 percent in 2006, which would bring Guangzhou's minimum wage to RMB 800 (USD 100). In the Qingyuan Shoetown factory, the starting take-home pay is RMB 650 (USD 81) per month. (Company payments, which include insurance and pension contributions, bring the total to RMB 1220 [USD 153].) With the rush of new factories to Qingyuan, however, this wage will not stay competitive for long. Most of the laborers and factory workers that we spoke with in the area earn RMB 700-900 (USD 88-113). A large banner outside what appeared to be a textile factory in Qingyuan offered RMB 900 (USD 113) as a starting salary.

18. (U) A reliable supply of labor is not assured either, as many of the workers in Qingyuan's factories are migrants. The Shoetown manager said the majority of his employees come

from inland provinces, such as Hunan, and only 30 percent are locals. These migrant laborers have more options than in the past, when Guangdong was the only place in China for factory jobs. Better wages and working conditions have convinced large numbers of laborers to travel to the Yangzi Delta and other industrializing regions instead. Indeed, Qingyuan's Yi Li electronics factory has reportedly only been able to find enough workers to fill half of its 30,000 openings, and a large banner outside the factory gate announces job opportunities.

¶9. (SBU) So how long before these new factories, faced with the same problems that forced them to leave the PRD -- including rising wages and energy shortages -- decide to move to new and cheaper locales? Five years at the most, according to the Shoetown manager. By that time, he said, his factory will likely relocate further inland, or possibly outside of China, to India, Vietnam, or Indonesia.

The Down Side: Pollution

¶10. (U) With a new emphasis on sustainable development and innovation in China's 11th Five-Year Plan, PRD officials are more willing to see polluting factories depart in order to make room for clean and high-tech companies. For example, approximately 1,000 PRD factories (including those involved in electroplating, dyeing, and paper-making) will reportedly need to comply with stringent new safety and environmental requirements by the end of 2006 or be forced to leave. Investors, including many from Hong Kong, are resigned to the fact that PRD officials are serious this time, and are looking to places outside of the PRD to invest -- Qingyuan being one.

¶11. (U) Qingyuan has seen a large number of ceramics factories open in the last couple of years. These factories emit high levels of pollutants into the air and use clay stripped from nearby hills -- both of which we witnessed

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during our stay. A recent Hong Kong study identified ceramics factories and automobiles as the two largest contributors to pollution in the Guangzhou area.

¶12. (U) In addition, local environmental authorities in Qingyuan and other less developed areas in South China, who are mindful of the importance of this new investment, have a reputation as being lax in their enforcement. In December 2005, a smelting factory in northern Guangdong's Shaoguan discharged 1,000-tons of cadmium-carrying waste into the Beijiang River during facility maintenance, forcing Qingyuan cities to use back-up water supplies (Reftel A). Officials took five days to notify the public about the incident, and the owner of the offending smelter told the press that any number of factories along the river could have been responsible.

Eco-Tourism Firms Find a Foothold

¶13. (U) Qingyuan is scenic area, blessed with forested mountains and abundant rivers. It is also home to a small but successful eco-tourism industry. Prefecture maps and hotel pamphlets tout the area's white-water rafting, and a mountain not far from Qingcheng has an "adventure" hiking trail, complete with chain bridges and pulley swings. Workers were clearing a road through a bamboo forest on a mountain north of Qingyuan that will provide access to a nearby river for rafting. Another successful venture is a 3,000 mu (494 acre) farm outside of Qingcheng, run by an overseas Chinese from Malaysia, which charges visitors RMB 25 (USD 3.13) to pick a variety of native and exotic fruits and vegetables.

¶14. (U) Eco-tourism is a dependable long-term industry for

Qingyuan, and tourists will continue to grow as the PRD and other areas of South China become more interconnected. Nevertheless, industrial development and pollution threaten to extinguish eco-tourism in its infancy, at least in the south where the majority of development is taking place. The mountainous north, which has less appeal to industry and more pristine land, stands to benefit greatly if these types of enterprises can attract enough customers.

Comment: A Hard Bargain

15. (SBU) Qingyuan's breakneck industrialization is bringing prosperity to a formerly poor, agricultural prefecture. Jobs are now abundant, and wages are rising. For companies, Qingyuan is a good compromise: it is located within two hours of Guangzhou and offers numerous investment incentives. Qingyuan's good times may be short-lived, however, as these factories are by no means wedded to it -- as the Nike manager said, within five years some of them will move again, taking their jobs with them and leaving behind abandoned buildings and polluted air and water. Migrant laborers from the interior will follow the factories elsewhere. Those who stay behind will need to figure out a more sustainable model for economic growth.

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